STATE OF CALIFORNIA

OFFICE OF ADMINISTRATIVE LAW

2007 OAL DETERMINATION NO. 6
(OAL FILE # CTU 06-0927-01)

REQUESTED BY: INDEPENDENT BROKERS AND AGENTS OF THE WEST

AGENCY: DEPARTMENT OF INSURANCE

CONCERNING: DECLARATION OF A SETTLEMENT AGREEMENT WITH AMERICAN RELIABLE INSURANCE COMPANY AS A PRECEDENT DECISION

DETERMINATION ISSUED PURSUANT TO GOVERNMENT CODE SECTION 11340.5.

SCOPE OF REVIEW

A determination by the Office of Administrative Law (OAL) evaluates whether or not an action or enactment by a state agency complies with California administrative law governing how state agencies adopt regulations. Nothing in this analysis evaluates the advisability or the wisdom of the underlying action or enactment. Our review is limited to the issue of whether the challenged rule is an "underground regulation" pursuant to Government Code section 11340.5[1] and Title 1, California Code of Regulations, section 250, and must, therefore be adopted pursuant to the Administrative Procedure Act (APA). OAL has neither the legal authority nor the technical expertise to evaluate the underlying policy issues involved in the subject of this determination.

ISSUE

OAL must determine whether the designation by the Department of Insurance (Department) of the Decision and Order in the Matter of American Reliable Insurance Company (Decision and Order) as a precedent decision pursuant to Government Code section 11425.60, subdivision (b), creates an underground regulation. The sole issue is the possible creation of an underground regulation. The content of the Decision and Order and the Decision Designating a Precedent Decision (Order) are not within the scope of our review, except as they might result in an underground regulation.

DETERMINATION

OAL determines that the effect of the Order by the Department designating its Decision and Order in the Matter of American Reliable Insurance Company as a precedent decision pursuant to Government Code section 11425.60(b) is to create an underground regulation.

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[1] Unless otherwise specified, all references are to the California Government Code.

FACTUAL BACKGROUND

On May 9, 2006, the Department served a "Notice of Noncompliance and Order to Show Cause" on the American Reliable Insurance Company (American Reliable). On June 30, 2006, the Department and American Reliable entered into a "Special Notice of Defense" (settlement agreement). This Special Notice of Defense resolved the issues raised by the Order to Show Cause. It stated that the "...attached Decision and Order will be issued by the Commissioner without the taking of proof and without a hearing or further adjudication of any question of fact or law."[2] American Reliable "waiv[ed] its right to attempt to set aside or vacate any provision of [the] Special Notice of Defense or the Decision and Order to be issued pursuant thereto, including by petition for any form of judicial administrative review on any grounds whatsoever."[3]

This settlement between the Department and American Reliable was based upon the conclusion by the Department that Cabrillo General Insurance Agency, Inc. and Superior Access Insurance Services had acted as American Reliable's agents pursuant to the definition of "insurance agent" in Insurance Code sections 31 and 1621.[4]

The Department declared the Decision and Order to be a precedent decision. The Decision and Order states:

> The word "producer"' is an industry term of art that refers to both insurance agents and insurance brokers. Insurance agents and insurance brokers both transact insurance by soliciting, negotiating, and/or executing insurance contracts. However insurance agents (as defined in sections 31 and 1621 [of the Insurance Code] differ from insurance brokers (as defined in sections 33 and 1623) [of the Insurance Code]. ... Whether a producer is an agent or broker depends on the nature of the producer's relationship with the insurance company with which the producer places a particular client.
>
> Under section 1731 [of the Insurance Code], a producer acts as an insurance agent in a particular transaction when it is appointed as an agent of an insurer pursuant to section 1704 [of the Insurance Code]. A producer also acts as an insurance agent in a particular transaction when it should be appointed as an agent, even if it is not appointed. A producer should be appointed as an agent of an insurer if the producer would be deemed an agent of that insurer under common law, i.e., if the producer represents or acts on behalf of an insurer, *inter alia*, ...

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[2] Special Notice of Defense, File No.: DISP 06091926, Paragraph 2.
[3] Special Notice of Defense, File No.: DISP 06091926, Paragraph 4.
[4] In the Matter of American Reliable Insurance Company, Notice of Noncompliance Pursuant to California Insurance Code Section 1858.1, File No. DISP 06091926.

The Notice of Noncompliance and Order to Show Cause contained a list of factors that the Department used to distinguish between an insurance agent and an insurance broker. The Decision and Order repeated these factors verbatim. The list states that "[a] producer represents or acts on behalf of an insurer, *inter alia*, whenever..."

- the insurer has given the producer discretion to issue insurance binders;
- the insurer has obtained the producer's express or tacit agreement to apply specific underwriting or rating factors before submitting applications to the insurer;
- the insurer has directed or controlled the producer in any respect or reserved the right to do so;
- the insurer has permitted the producer to display the insurer's name or logo on the producer's signage, stationery or business cards in a manner that implies ostensible agency;
- the insurer refers potential or existing insureds to the producer;
- the insurer refers the producer to potential or existing insured;
- the insurer attempts to control the licensee's conduct by disciplining the licensee (other than by terminating), or maintaining the right to discipline him, for failing to follow the insurer's rules or for failing to meet production standards;
- the insurer provides the same or substantially similar training to supposed brokers as to any appointed agents;
- the relationship between the producer and the insurer is functionally indistinguishable from the relationship between the insurer and its appointed agents;
- the producer has placed the insurer's interests above that of the insured and the insurer has accepted the benefits thereof; or
- the insurer has incentivized the producer to act upon the insurer's behalf by promising to provide compensation contingent upon the producer meeting a premium volume threshold, loss ratio, or level of profitability.[5]

On June 30, 2006, the same day that the Special Notice of Defense and the Decision and Order were issued, the Department issued an "Order Designating Decision as Precedential", which stated that the "American Reliable Decision and Order is hereby designated as a precedential decision pursuant to California Government Code Section 11425.60, subdivision (b), effective immediately."

It is this Order that the petitioner challenges as creating an underground regulation.

PETITIONER'S ARGUMENT

Petitioner is a trade association representing independent insurance agents and insurance brokers in California, Oregon, Washington and Alaska. The Petitioner:

> seeks a determination, under California Government Code § 11340.5 and California Administrative Code Title 1, § 260(a), that the Department may not

[5] Decision and Order, page 4.

'issue, utilize, enforce, or attempt to enforce,' the American Reliable order or any other order purporting to confer precedential status on a 'decision' reached by way of a settlement agreement, a 'Special Notice of Defense,' or any equivalent document or procedure. (Emphasis added.)

The petitioner also argues that the Decision and Order in American Reliable does not fall under any express exemption from the APA. Specifically, the Petitioner argues that the exemption cited by the Department, section 11425.60(b), which states that the designation of a decision or part of a decision as a precedent decision is not a rulemaking and need not be done under Chapter 3.5 (commencing with 11340), does not apply to settlement-type decisions. The Petitioner argues that section 11425.60 applies only to adjudicative decisions that emerge from an adversarial hearing in which the decision-maker is exposed to differing viewpoints about the facts and the applicable laws and then renders a decision based on his factual and legal findings.

DEPARTMENT'S RESPONSE

The Department sent OAL a letter setting forth its arguments against accepting the petition. After OAL accepted the petition, at the request of the Department this letter was incorporated as the Department's Response to the petition. The Department's position is that:

- Government Code section 11425.60(b) is unambiguous and OAL may not construe a facially unambiguous statute;
- Government Code section 11425.60(b) exempts all precedent decisions from the APA, not merely precedent decisions that lack one or more stipulations of fact or law, ("expressio unis (sic) est exclusio alterius" theory);
- even if Government Code section 11425.60 (b) were ambiguous, it is permissible for decisions based on stipulations to be designated as precedent;
- if section 11425.60 is ambiguous, that ambiguity can be and should be addressed by the Legislature rather than by OAL;
- petitioner's policy arguments against precedent decision following settlement may not be considered; and
- OAL should not "meddle" in another agency's precedent decisions.

UNDERGROUND REGULATIONS

Section 11340.5, subdivision (a), prohibits state agencies from issuing rules unless the rules comply with the APA. It states, in part:

(a) No state agency shall issue, utilize, enforce, or attempt to enforce any guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule, which is a regulation as defined in Section 11342.600, unless the guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule has been adopted as a regulation and filed with the Secretary of State pursuant to [the APA].

When an agency issues, utilizes, enforces, or attempts to enforce a rule in violation of section 11340.5 it creates an underground regulation. "Underground regulation" is defined in Title 1, California Code of Regulations, section 250, as follows:

> "Underground regulation" means any guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule, including a rule governing a state agency procedure, that is a regulation as defined in Section 11342.600 of the Government Code, but has not been adopted as a regulation and filed with the Secretary of State pursuant to the APA and is not subject to an express statutory exemption from adoption pursuant to the APA.

OAL is empowered to issue its determination as to whether or not an agency employs an underground regulation pursuant to section 11340.5 subdivision (b). An OAL determination that an agency is using an underground regulation is not enforceable against the agency through any formal administrative means, but it is entitled to "due deference"[6] in any subsequent litigation of the issue.

ANALYSIS

To determine that an agency is in violation of section 11340.5, it must be demonstrated that the alleged underground regulation is a regulation as defined by section 11342.600, that it has not been adopted pursuant to the APA, and that it is not subject to an express statutory exemption from the APA.

A regulation is defined in section 11342.600 as:

> . . . every rule, regulation, order, or standard of general application or the amendment, supplement, or revision of any rule, regulation, order, or standard adopted by any state agency to implement, interpret, or make specific the law enforced or administered by it, or to govern its procedure.

In *Tidewater Marine Western Inc. v. Victoria Bradshaw,* (1996)14 Cal.4th 557, 571, [59 Cal.Rptr.2d 186] the California Supreme Court found that:

> A regulation subject to the Administrative Procedure Act (APA) (Gov. Code § 11340 et seq.) has two principal identifying characteristics. First, the agency must intend its rule to apply generally, rather than in a specific case. The rule need not, however, apply universally; a rule applies generally so long as it declares how a certain class of cases will be decided. Second, the rule must implement, interpret, or make specific the law enforced or administered by the agency, or govern the agency's procedure (Gov. Code § 11342 subd. (g).)

First element of *Tidewater*

[6] Grier v. Kizer (1990) 219 Cal.App.3d 422, 268 Cal.Rptr. 244

The first element of a regulation identified in *Tidewater* is whether the rule applies generally. For an agency rule to be a "standard of general application," it need not apply to all citizens of the state. It is sufficient if the rule applies to all members of a class, kind, or order.[7]

In this case, the Department has declared its settlement decision to be a precedent decision. Pursuant to section 11425.60, a decision "may not be expressly relied upon as precedent unless it is designated as a precedent decision by the agency." By declaring the settlement decision to be precedent, the Department has expressly stated its intention to expand the effect of the settlement beyond American Reliable and apply the decision to others in similar circumstances.

If the challenge were to the Decision and Order itself, it would not meet the *Tidewater* requirement for a "standard of general application" because a settlement between the Department and American Reliable is not a "...rule, regulation, order, or standard of general application..." It is the act of declaring that settlement a precedent decision that transforms it into a standard of general application. The Order Designating Decision as Precedent thereby functionally incorporates the Decision and Order by reference and changes it from being a compromise between two parties into a "...rule, regulation, order, or standard of general application." Viewed separately neither the Decision and Order nor the one sentence Order Designating Decision is a regulation, but together the effect is synergistic.

The first element of *Tidewater*, therefore, has been met.

Second element of *Tidewater*

The second element of *Tidewater* is that the rule must implement, interpret or make specific the law enforced or administered by the agency, or govern the agency's procedure.

The Department of Insurance is an independent department headed by the Insurance Commissioner (Commissioner), an elected official.[8] The Commissioner "...shall perform all duties imposed upon him or her by the provisions of [the Insurance Code] and other laws regulating the business of insurance in [California], and shall enforce the execution of those provisions and laws."[9]

The Department's 0Decision and Order reiterates the factors listed above in Factual Background, which distinguish between an agent and a broker. We find that these factors implement, interpret or make specific those sections of the Insurance Code enforced or administered by the Department.

The second element of *Tidewater*, therefore, has been met.

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[7] Roth v. Department of Veteran Affairs (1980) 110 Cal.App.3d 622, 630, 167 Cal.Rptr. 552, 556; see Faulkner v. California Toll Bridge Authority (1953) 40 Cal.2d 317, 323-324 (a standard of general application applies to all members of any open class).)

[8] Insurance Code section 12900.

[9] Insurance Code section 12129

Exemptions From The APA

Generally, all regulations adopted by state agencies are required to be adopted pursuant to the APA, unless expressly exempted by statute.[10] In *United Systems of Arkansas v. Stamison* (1998) 63 Cal.App.4th 1001, 1010 [74 Cal.Rptr.2d 407, 411-12] review denied, the California Court of Appeal rejected an argument by the Director of the Department of General Services that language in the Public Contract Code had the effect of exempting rules governing bid protests from the APA.

According to *Stamison*:

> ***When the Legislature has intended to exempt regulations from the APA, it has done so by clear, unequivocal language.*** (See, e.g., Gov. Code, section 16487 ['The State Controller may establish procedures for the purpose of carrying out the purposes set forth in Section 16485. These procedures are exempt from the Administrative Procedure Act.']; Gov. Code, section 18211 ['Regulations adopted by the State Personnel Board are exempt from the Administrative Procedure Act']; Labor Code, section 1185 [orders of Industrial Welfare Commission 'expressly exempted' from the APA].) [Emphasis added.][11]

The Department argues that its designation of the *American Reliable* Decision and Order is exempt from the requirements of the APA pursuant to Government Code section 11425.60, subdivision (b), which states:

> (b)... Designation of a decision or part of a decision as a precedent decision is not rulemaking and need not be done under Chapter 3.5 (commencing with Section 11340).

Section 11425.60, which establishes an express exemption from the APA, is found in Chapter 4.5, Article 6, entitled Administrative Adjudication Bill of Rights. The Department argues that this exemption is unambiguous on its face and cannot be construed by OAL. The Department's position is that the statute refers to a "decision or part of a decision" and that is the end of the matter. However, the discussion of ambiguity is not limited to one code section in isolation. Ambiguity may arise in the interaction of various code sections in the Administrative Adjudication provisions of the APA as well as with the Administrative Regulations and Rulemaking portions of the APA. In *Henning v. Division of Occupational Safety and Health* (1990) 219 Cal.App.3d 747, 763 [268 Cal.Rptr. 476, 485] the Third District Court examined this issue in depth as they explained that:

> ...courts are especially reluctant to find an implied repeal of statutes that serve an important public purpose. (*Western Oil and Gas Assn. v. Monterey Bay Unified*

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[10] Government Code section 11346.

[11] 63 Cal.App.4th at 1010, 74 Cal.Rptr.2d at 411.

Air Pollution Control Dist., supra, 49 Cal.3d 408, 419, 261 Cal.Rptr. 384, 777 P.2d 157.)

The court continued by quoting Sutherland on statutory construction:

> ...[l]egislation never is written on a clean slate, nor is it ever read in isolation or applied in a vacuum. Every new act takes its place as a component of an extensive and elaborate system of written laws. ' (2A Sutherland, Statutory Construction (4th ed. 1984 rev.) Section 53.01 p. 549.) In such a legal system, harmony and consistency are positive values 'because they serve the interests of impartiality and minimize arbitrariness. Construing statutes by reference to others advances those values. In fact, courts have been said to be under a duty to construe statutes harmoniously where that can reasonably be done.' (*Op. cit. supra*, at pp. 549-550.) It follows that the principle that related statutes should be construed harmoniously 'is a restatement of the presumption against the implied repeal of statutes' (*Op. cit. supra*, section 51.01, p. 451.) If found to be in irreconcilable conflict, only the most recent statute can survive and the earlier one is deemed to have been repealed by implication. (*Estate of McGee* (1908) 154 Cal. 204, 207, 97 P.299.) The rule of harmony then is designed to avert such an implied repeal. But its office is not to treat words of one statute as if they were useless surplusage. Thus, "[w]ords must be construed in context, and statutes must be harmonized both internally and with each other, to the extent possible. Interpretative construction which render some words surplusage, defy common sense, or lead to mischief or absurdity, are to be avoided. (*California Mfrs. Assn. V. Public Utilities Com.* (1979) 24 Cal.3d 836, 844, 157 Cal.Rptr. 676, 598 P.2d 836, citations omitted.)"

OAL has the authority to determine if a challenged rule is an underground regulation and statutory analysis is a requisite part of that process. OAL must therefore examine whether the exemption in section 11425.60(b) can be read harmoniously together with other applicable statutes to include a non-adjudicative decision, such as the *American Reliable* Decision and Order, within the scope of a precedent decision. The Department's arguments that OAL should not "meddle" in another agency's precedent decisions and that if section 11425.60 is ambiguous, that ambiguity can be and should be addressed by the Legislature rather than by OAL, would preclude all agencies from ever determining if statutory language is ambiguous. If an ambiguity exists then legislative intent is considered "... and the purposes sought to be achieved and evils to be eliminated may have an important place in ascertaining legislative intent..."[12] OAL is not "meddling" when it is fulfilling its statutory duties.

[12] Bethlehem Pacific Coast Steel Corporation v. Franchise Tax Board (1962) 203 Cal.App.2d 458, 463, 21 Cal.Rptr 707, 710.

Ambiguity

In *People v. Superior Court of San Joaquin County Respondent; Jose Francisco Zamudio, Real Party in Interest* (2000) 23 Cal.4th 183, 192-193 [96 Cal.Rptr. 2d 463] (referred to hereafter as *Zamudio*), the California Supreme Court set forth the following analytical framework:

> ...Initially, '[a]s in any case of statutory interpretation, our task is to determine afresh the intent of the Legislature by construing in context the language of the statute.' (*Harris v. Capital Growth Investors XIV* (1991) 52 Cal.3d 1142, 1159, 278 Cal.Rptr. 614, 805 P.2d 873) In determining such intent, we begin with the language of the statute itself. (*Rojo v. Kliger* (1990) 52 Cal.3d 65, 73, 276 Cal. Rptr. 130, 801 P.2d 373.) That is, we look first to the words the Legislature used, giving them their usual and ordinary meaning. (*City of Santa Cruz v. Municipal Court* (1989) 49 Cal.3d 74, 90, 260 Cal.Rptr. 520, 776 P.2d 222.) 'If there is no ambiguity in the language of the statute, 'then the Legislature is presumed to have meant what is said, and the plain meaning of the language governs.' *Lennane v. Franchise Tax Bd.* (1994) 9 Cal.4th 263, 268, 36 Cal.Rptr.2d 563, 885 P.2d 976.) But when the statutory language is ambiguous, 'the court may examine the context in which the language appears, adopting the construction that best harmonizes the statute internally and with related statutes.' (*Calvillo-Silva v. Home Grocery* (1998) 19 Cal.4th 714, 724, 80 Cal.Rptr.2d 506, 968 P.2d 65.)

In *Paleski v. State Department of Health Services* (2006) 144 Cal.App.4th 713, 51 [Cal.Rptr.3d 28, 06] the Second District Court of Appeal further explained the plain meaning rule:

> ....However, the 'plain meaning rule does not prohibit a court from determining whether the literal meaning of a statute comports with its purpose....If the terms of the statute provide no definitive answer, then courts may resort to extrinsic sources, including the ostensible objects to be achieved and the legislative history.... 'We must select the construction that comports most closely with the apparent intent of the Legislature, with a view to promoting rather than defeating the general purpose of the statute, and avoid an interpretation that would lead to absurd consequences....The legislative purpose will not be sacrificed to a literal construction of any part of the statute....' (*Bodell Construction Co. v. Trustees of Cal. State University* (1998) 62 Cal.App.4th 1508, 1515-1516, citations omitted.)

Therefore, the first step in the discussion of ambiguity is to examine the language of the relevant statutes. Chapter 4.5, Article 6, entitled Administrative Adjudication Bill of Rights, section 11425.60, which is captioned "Precedent; designation; index", declares that:

> (a) A ***decision may not be expressly relied on as precedent unless it is designated as a precedent decision by the agency.***

> ***(b) An agency may designate as a precedent decision a decision or part of a decision that contains a significant legal or policy determination of general application that is likely to recur. Designation of a decision or part of a decision as a precedent decision is not rulemaking and need not be done under Chapter 3.5 (commencing with Section 11340).*** An agency's designation of a decision or part of a decision, or failure to designate a decision or part of a decision, as a precedent decision is not subject to judicial review....(Emphasis added.)

The Department's response to the petition, dated October 25, 2006, asserts that the language of section 11425.60 ("precedent decision") does not exclude a "decision by settlement" and therefore "...one must apply the doctrine of expressio unis (sic) est exclusio alterius." *Black's Law Dictionary*, 7th Edition, page 602, states this doctrine is "[a] canon of construction holding to express or include one thing implies the exclusion of the other, or of the alternative...." In *People v. Saunders* (*supra*), however, the Fifth District Court of Appeal explained that the rule of expressio unius est exclusio alterius is "subordinate to the primary rule that legislative intent governs interpretation of a statute." (*In re Joseph B.* (1983) 34 Cal.3d 952, 957, 196 Cal.Rptr. 348, 671 P.2d.852.)" Statutory language may be ambiguous on its face or it may "...have a latent ambiguity such that it does not provide a definitive answer." (*Casterson v. Superior Court of Santa Cruz County* (2002) 101 Cal.App. 4th 177, 187 [123 Cal.Rptr. 2d 637]

Therefore the fact that section 11425.60 does not exclude non-adjudicative decisions is not dispositive, and the question remains: What "decisions" qualify to be precedent decisions?

The statute which authorizes a decision by settlement is contained in Chapter 4.5, Article 4, Governing Procedure, section 11415.60, titled Decision by Settlement and provides in subdivision (a) that:

> An agency ***may formulate and issue a decision by settlement pursuant to an agreement of the parties, without conducting an adjudicative proceeding.*** Subject to subdivision (c), the settlement may be on any terms the parties determine are appropriate. Notwithstanding any other provision of law, no evidence of an offer of compromise or settlement made in settlement negotiations is admissible in an adjudicative proceeding or civil action, whether as affirmative evidence, by way of impeachment, or for any other purpose, and no evidence of conduct or statements made in settlement negotiation is admissible to provide liability for any loss or damage except to the extent provided in Section 1152 of the Evidence Code. Nothing in this subdivision makes inadmissible any public document created by a public agency. (Emphasis added.)

The statutes governing adjudicative decisions are contained in Chapter 4.5, Article 6, entitled Administrative Adjudication Bill of Rights. Section 11425.10 requires:

(a) The governing procedure by which an agency conducts an adjudicative proceeding is subject to all of the following requirements:

....

(6) The decision shall be in writing, be based on the record, and include a statement of the factual and legal basis of the decision as provided in Section 11425.50.

(7) A decision may not be relied on as a precedent unless the agency designates and indexes the decision as precedent as provided in Section 11425.60.

....

Section 11425.50 requires:

(a) The decision shall be in writing and shall include a statement of the factual and legal basis for the decision.

....

(c) The statement of the factual basis for the decision shall be based exclusively on the evidence of record in the proceeding and on matters officially noticed in the proceeding. The presiding officer's experience, technical competence, and specialized knowledge may be used in evaluating evidence.

As noted above, the authorization to issue a decision by settlement is contained in Chapter 4.5, Article 4, Governing Procedure. The sections setting forth requirements for adjudicative proceedings and the APA exemption for precedent decisions are both found in Article 6, Administrative Adjudication Bill of Rights. We find it significant that section 11425.50 requires "the decision shall be in writing and shall include a statement of the factual and legal basis for the decision. ...The statement of the factual basis for the decision shall be based exclusively on the evidence of record in the proceeding...", all of which are elements not contained in a non-adjudicative settlement. There is no record or proceeding in a non-adjudicative settlement. An ambiguity exists as to whether a "decision by settlement" comes within the meaning of a "decision" in section 11425.60.

Statutory language can also be examined for ambiguity by following the analysis contained in *Zabetian v. Medical Board of California* (2000) 80 Cal.App.4th 462, 467 [94 Cal.Rptr.2d 917]. The Third District Court of Appeal explained:

When statutory language is clear and unambiguous, there is no need for construction and courts should not indulge in it." (*People v. Overstreet* 1986) 42 Cal.3d 891, 895, 231 Cal.Rptr. 213, 726 P.2d 1288.) Whether that is the case can be determined only when the language is sought to be applied to the case at hand. Each party will normally advance a candidate meaning of consequence to the party's position. ***If it cannot be determined from the language of the statute which is the correct application, extrinsic aids may be employed bearing on the objects to be achieved, the evils to be remedied, and the legislative history of the enactment.*** (*Long Beach Police Officers Assn. City of Long Beach* (1988) 46

> Cal.3d 736, 741, 250 Cal.Rptr. 869, 759 P.2d 504.) We call this an inquiry into legislative intent, i.e., an inquiry into the plausible meanings to be ascribed to the language in view of the history and context of the legislation. It does not sanction a judicial construction predicated upon a perceived policy which is not within the semantic constraints of the statutory language.... (Emphasis added)

Because of the latent ambiguities OAL finds in the sections quoted above, it is necessary and proper to determine the legislative intent to resolve the meaning of section 11425.60.

Legislative Intent

The California Supreme Court in *Conservatorship of Wendland* (2001) 26 Cal.4th 579, 110 Cal.Rptr.2d 412, 430, stated that "... [e]xplanatory comments by a law revision commission are persuasive evidence of the intent of the legislature in subsequently enacting its recommendation into law. (*Brian W. v. Superior Court* (1978) 20 Cal.3d 618, 623, 143 Cal.Rptr. 717, 574 P.2d 788.)" Law Revision Commission Comments are usually a reliable guide to legislative intent. (*In re Bryce C.* (1995) 12 Cal 4th 226, 241, 48 Cal.Rptr.2d 120)

The California Law Revision Commission commented on section 11425.60 (precedent decisions) that "...The first sentence of subdivision (b) recognizes the need of agencies to be able to make law and policy through ***adjudication as well through rulemaking.*** It codifies the practice of a number of agencies to designate important decisions as precedential.... Section 11425.60 is intended to encourage agencies to articulate what they are doing ***when they make new law or policy in an adjudicative decision.*** An agency may not by precedent decision revise or amend an existing regulation or adopt a rule that has no adequate legislative basis."[13] (Emphasis added.) Section 11405.20 defines "adjudicative proceeding" as "...an evidentiary hearing for determination of facts pursuant to which an agency formulates and issues a decision."

The Law Revision Commission reiterated that "the precedent decision provision recognizes ***that agencies make law and policy through administrative adjudication as well as through rulemaking.***"[14] (Emphasis added.)

The Law Revision Commission's Comments regarding section 11415.60 (Decision by settlement) state that "subdivision (a) of section 11415.60 [decision by settlement] codifies the rule in *Rich Vision Centers, Inc. v. Board of Medical Examiners*, 144 CalApp.3d 110, 192, Cal.Rptr. 455 (1983)."[15] In the *Rich* case the Second District Court of Appeal identified the issue as whether the Board of Medical Examiners "...had the authority to engage in settlement negotiations of pending cases, the resolution of which called for payment of attorneys fees and future investigation costs by litigants." The court held that "... the Board had the implied power to settle licensing disputes." (*Rich Vision Centers v. Board of Medical Examiners, supra*)

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[13] 25 Cal.L.Rev.Comm.Reports 55, 163 (1995)
[14] 25 Cal.L.Rev.Comm.Reports 55, 103 (1995)
[15] 25 Cal.L.Rev.Comm.Reports 55, 150.(1995)

It is interesting to note that the word "decision" appears only once in the *Rich* case as a title: "Pursuant to the negotiated settlement, the deputy attorney general drafted a '***Stipulation and Decision***' covering the administrative matters and other required documents necessary for the civil proceedings." (Emphasis added.) The court referred to "negotiated settlement" and "settlement negotiation." The phrase "decision by settlement" appears nowhere in the case. As the *Rich* court explained:

> The ability to negotiate favorable settlement terms has long been among attorneys most effective tools for promoting their clients best interests. To successfully use this tool however, an attorney must have flexibility in formulating the terms and conditions of any agreement to maximize benefit to the client. ***Settlement negotiations involve give and take, and the final agreement is a compromise.*** Government attorneys no less than attorneys in the private sector are responsible for promoting their clients best interests. (See *People ex rel. Deukmejian v. Brown* (1981) 29 Cal.3d 150, 157, 172 Cal.Rptr. 478, 624 P.2d 1206.) There is no reason to handicap those members of the Attorney General staff ***who represent licensing agencies*** in performing their duty by limiting their ability to propose and include any settlement term beneficial to the public. (Emphasis added.)

Because section 11415.60 codifies the *Rich* holding, which characterizes final settlement agreements as a "compromise" – a nonadjudicative proceeding, it is clear the Legislature did not envision such decisions would be governed by the procedures and protections that apply to adjudicative proceedings found in section 11425.10. Section 11425.10 was enacted at the same time section 11415.60 was enacted (Stats. 1995, c. 938, sec. 21). Section 11415.60 specifically states that adjudicative proceedings are not conducted. Furthermore, it is only the decisions that result from adjudicatory proceedings conducted pursuant to the governing procedures of section 11425.10 that the Legislature intended to be allowed to be designated a "precedent decision."

Further evidence of Legislative intent can be found in the organization of Chapter 4.5. The provisions discussing decisions by settlement in section 11415.60 are found in Chapter 4.5, Article 4, Governing Procedure. However, the provision permitting the designation of a precedent decision, section 11425.60, is in Article 6, entitled "Administrative Adjudicative Bill of Rights" (sections 11425.10 through 11425.60). The Bill of Rights contains the minimum due process and public interest requirements for adjudicative hearings subject to Chapter 4.5.

In *In re Carr* (1998) 65 Cal.App.4th 1525, 1530 [77 Cal.Rptr.2d 500] the Second District Court of Appeal explained that:

> ...chapter and section headings in statutes may be considered in determining legislative intent. The California Supreme Court has held: "However, it is well established that 'chapter and sections headings [of an act] may properly be considered in determining legislative intent" [citation], and are ***entitled to considerable weight.*** [Citation.] [Citations.]" (Citations omitted) (Emphasis added)

The fact that section 11415.60 authorizing a decision by settlement is in Article 4, Governing Procedures, and section 11425.60, the APA exemption for precedent decisions, is in Article 6, Administrative Adjudication Bill of Rights, supports our conclusion that the Legislature intended to limit the exemption for precedent decisions to adjudicative proceedings.

In addition to the Legislative intent expressed in the Law Revision Commission's Comments, it is also permissible to examine the purposes of the entire APA. In *Bethlehem Pacific Coast Steel Corporation v. Franchise Tax Board* (1962) 203 Cal.App.2d 458, 463 [21 Cal.Rptr. 707, 710], the Third District Court of Appeal explained that:

> One of the many rules laid down in aid of statutory interpretation is that legislative intent should be gathered from the whole Act and reconciled with reasonable application to carry out the policy and purpose of the legislation. (*Select Base Materials v. Board of Equalization*, 51 Cal.2d 640, 335 P.2d 672; *County of Alameda v. Kuchel*, 32 Cal.2d 193, 195 P.2d 17; *Warner v. Kenny*, 27 Cal.2d 627, 165 P.2d 889.)
>
> . . .
>
> Of course, it is axiomatic that the purposes sought to be achieved and evils to be eliminated may have an important place in ascertaining legislative intent. (*California Drive-In Restaurant Ass'n v. Clark*, 22 Cal.2d 287, 140 P.2d 657, 147 A.L.R. 1028; *Freedland v.Greco*, 45 Cal.2d 462, 289 P.2d 463.)

In *Tidewater (supra* at p. 193) the California Supreme Court emphasized the importance of public participation in the rulemaking process.

> One purpose of the APA is to ensure that those persons or entities whom a regulation will affect have a voice in its creation (*Armistead v. State Personnel Board* (1978) 22 Cal.3d 198, 204-205, 149 Cal.Rptr. 1, 583 P.2d 744(*Armistead*)), as well as notice of the law's requirement so that they can conform their conduct accordingly (*Ligon v. State Personnel Bd.* (1981) 123 Cal.App.3d 583, 588, 176 Cal.Rptr. 717 (*Ligon*)). The Legislature wisely perceived that the party subject to regulation is often in the best position, and has the greatest incentive, to inform the agency about possible unintended consequences of a proposed regulation. Moreover, ***public participation in the regulatory process directs the attention of agency policymakers to the public they serve, thus providing some security against bureaucratic tyranny.*** (See *San Diego Nursery Co. v. Agricultural Labor Relations Bd.* (1979) 100 Cal.App.3d 128, 142-143, 160 Cal.Rptr. 822.) (Emphasis added.)

We also examine the "purposes sought to be achieved and evils to be eliminated"[16] in the adoption of the provisions in Chapter 4.5, Article 6, Administrative Adjudication Bill of Rights,

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[16] *Bethlehem Pacific Coast Steel Corporation v. Franchise Tax Board, supra.*

These purposes are described in the Law Revision Commission's Comments regarding section 11425.60:[17]

> The proposed law includes an 'administrative adjudication bill of rights' that prescribes ***fundamental due process and public policy protection for person involved in administrative adjudication by state agencies.*** These provisions are described below.
>
> **Notice and Opportunity To Be Heard**
> Notice to the person that is the subject of agency proceeding and an opportunity for the person to be heard are fundamentals of due process of law. The proposed law codifies this principle and makes clear that the opportunity to be heard includes the right of the person to present and rebut evidence. (Emphasis added)

The Comments describe other provisions of the Administrative Adjudication Bill of Rights including the following Comment regarding Precedent Decisions[18].

> **Precedent Decisions**
> The proposed law allows an agency to designate a decision as precedential if the decision contains a significant legal or policy determination that is likely to recur. The agency must maintain an index of determinations made in precedent decisions. An agency's designation of, or failure to designate, a decision as precedential is not judicially reviewable, but a decision that is not designated as precedential may not be cited as precedent.
>
> The precedent decision provision ***recognizes that agencies make law and policy through administrative adjudication as well as through rulemaking.*** Although agency decisions are public records, they are inaccessible to the public except in the case of the few existing agencies that publish their decision or designate precedent decisions.
>
> Extension of the precedent decision requirement to all agencies would make the decisions generally available and would benefit everyone, including counsel for both sides, as well as the presiding officers and agency heads who make the decisions. ***It would encourage agencies to articulate what they are doing when they make new law or policy in an administrative adjudication.*** Additionally, it is more efficient to cite an existing decision than to reconstruct the policy or even decide inconsistently without knowing or acknowledging that this has occurred.
> ....
> (Emphasis added.)

The specific language of the relevant provisions, the placement of the individual sections in the different Articles in Chapter 4.5, and the intent of the Legislature as evidenced by the Law

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[17] 25 Cal.L.Rev.Comm.Reports 55, 98-99
[18] 25 Cal.L.Rev.Comm.Reports 55, 103-104

Revision Commission Comments lead us to the conclusion that only decisions that are adjudicatory may be declared precedent.[19]

CONCLUSION

As the Law Revision Commission Comments make clear, there are two ways for agencies to make new law or policy: (1) APA rulemaking or (2) administrative adjudication which has been designated a precedent decision. The Department did not employ either method.

If OAL were to sanction the Department's interpretation that a decision by a non-adjudicative settlement reached by compromise between the agency and an individual party can be transformed into a precedent decision, the result would not only create a third rulemaking method not sanctioned by the Legislature, but would also effectively eviscerate the rulemaking portion of the APA. The most significant purposes of the APA rulemaking process could be circumvented by an agency placing new rules into a non-adjudicative "decision by settlement" and then declaring it a precedent decision. The Department's interpretation would impermissibly allow state agencies to circumvent the rulemaking process with impunity, precluding public participation, avoiding OAL review for substantive and procedural compliance with the APA, and providing no record for a court to review. In our view, such a result would nullify the APA.

By finding that the APA exemption for precedent decisions is limited to decisions reached by administrative adjudication and in compliance with the requirements of sections 11425.50 and 11425.60, OAL's determination harmonizes sections 11405.20, 11415.50 and 11425.60 both internally and also with the rulemaking requirements of the APA. Our determination preserves both the rulemaking and adjudicative portions of the APA, and reconciles the provisions with legislative intent.

For these reasons, OAL determines that the effect of the Order by the Department designating its Decision and Order in the Matter of American Reliable Insurance Company as a precedent

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[19] We additionally note that even adjudicative decisions may at times exceed the scope of the APA exemption set forth in section 11425.60. In *Rea v. Worker's Compensation Appeals Board* (2005) 127 Cal.App.4th 625, 647-648 [25 Cal.Rptr. 3d 828], the Second District Court of Appeal analyzed whether procedures contained in a adjudicative decision that had been declared a precedent decision were exempt from the APA or whether they were regulations. The court examined the procedures and determined that the decision had "adopted and announced a whole body of entirely new procedures." The court found that "the definition of regulation under Government Code section 11342.600 is more applicable to the new procedures ... than the definition of precedent decision under Government Code section 11425.60, subdivision (b)."
Because we find that the Legislature intended section 11425.60 to apply only to adjudicative decisions, there is no need for us to analyze whether the factors in the settlement agreement between the Department and American Reliable are of a scope or nature that might constitute a regulatory scheme comparable to that at issue in *Rea*.

decision pursuant to Government Code section 11425.60(b) is to create an underground regulation.

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